judgment, the proposed defence, as drafted, was doomed to fall.

Accordingly, for these reasons, the appeal was dismissed with costs.

*Appeal dismissed.*

Solicitors: *JB Jeyaretnam & Co; Lee & Lee.*

Reported by *Zarinah Marican*

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## Joo Yee Construction Pte Ltd (In Liquidation) v Diethelm Industries Pte Ltd & Ors

HIGH COURT (SINGAPORE) — ORIGINATING SUMMONS NO 958 OF 1989
THEAN J
1 MARCH 1990

*Contract — Building contract — Provision for direct payment to nominated sub-contractors by employer — Main contractor wound up — Whether provision binds the liquidators of main contractor*

*Companies and Corporations — Winding up — Application by liquidators to determine question whether direct payment provision contravenes company law — Companies Act (Cap 50, 1988 Ed), ss 280(1) & 327(2)*

A winding-up order was made against the plaintiff on 10 February 1989. On 12 September 1986, the plaintiff entered into a building contract ('the main contract') with the government of Singapore ('the government') for the construction of the Blood Transfusion Services/Department of Scientific Services Complex at the General Hospital, Singapore, and International Development and Consultancy Corp Pte Ltd ('Indeco') was appointed for the purpose of administering the main contract. The first, second, third and fourth defendants ('the four defendants') are the nominated sub-contractors for the development. Each of the four defendants, as the nominated sub-contractors, on diverse dates entered into a sub-contract with the plaintiff, and the terms of each sub-contract are identical in all material respects. In respect of works carried out by the plaintiff and the sub-contractors at various stages of the development, certificates of payment under cl 38 of the conditions of the main contract had been issued by Indeco for payments to be made to the plaintiff as the main contractor; included in the certificates were the amounts payable by the plaintiff to the nominated sub-contractors respectively for the works carried out and materials and goods supplied by them, and these amounts were set out in a list annexed to each of the certificates. Up to the date of commencement of liquidation of the plaintiff, 19 certificates had been issued, and payment of the full amount thereunder had been made to the plaintiff. Except in respect of two certificates, namely, certificate nos 16 and 17, the plaintiff had, on receipt of the amount under each certificate, paid the amounts stated in the list to the respective sub-contractors. In respect of certificate nos 16 and 17, though full amounts thereunder had been paid by the government to the plaintiff, certain amounts remain unpaid to the first, third and fourth defendants.

Since the payment under certificate no 19, no further certificate has been issued by Indeco. The plaintiff's liquidators took out this application for determination of whether upon the true construction of cl 20(e) of the main contract, any direct payment made pursuant to the said provision by the government to the four defendants would, having regard to the winding-up order being made against the plaintiff, be in contravention of s 329 of the Companies Act (Cap 50, 1985 Ed). The true issue before the court was whether any direct payment to be made by the government to the nominated sub-contractors pursuant to cl 20(e) of the main contract contravenes the combined operation of ss 280(1) and 327(2) of the Companies Act.

**Held**, interpreting the clause in favour of the plaintiff:

(1) Upon liquidation of an insolvent company (whether voluntary or compulsory), subject to the rights of preferential creditors and also secured creditors, if any, its property must be applied in settlement of its liabilities pari pasu, and any contract made by the company which provides for a distribution of any of its property for the benefit of one or more of its unsecured creditors which runs counter to or seeks to vary this rule is contrary to public policy, and the law as regards distribution of the insolvent's property under the insolvency legislation must prevail.

(2) If the government elects to make direct payment to the three defendants under cl 20(e) and in consequence deduct these amounts from moneys due or payable to the plaintiff, it is in effect distributing to the three unsecured creditors of the plaintiff sums of money which would otherwise be paid to the plaintiff and form part of the general assets of the plaintiff available for distribution among all its creditors pari pasu. Clearly, the operation of such a contractual provision in the liquidation of the plaintiff would infringe the insolvency law providing for distribution of the insolvent's property pari pasu among its creditors.

(3) If cl 20(e) of the main contract is invoked, it would in the circumstances contravene the combined operation of ss 280(1) and 327(2) of the Companies Act (Cap 50, 1985 Ed); the liquidator is not bound by that clause, and consequently any payment made thereunder to the sub-contractors is void as against him.

[*Editorial Note*: The first to fourth defendants have appealed to the Court of Appeal vide Civil Appeal No 31 of 1990. The fifth defendant has appealed vide Civil Appeal No 30 of 1990.]

**Cases referred to**

1 *Re Wilkinson, ex p Fowler* [1905] 2 KB 713 (not folld)
2 *Re Tout and Finch Ltd* [1954] 1 All ER 127 (not folld)
3 *Re CG Monkhouse Pty Ltd (in liquidation) and the The Companies Act* [1968] 88 WN (Pt 2) (NSW) 238 (not folld)
4 *British Eagle International Airlines Ltd* v *Compagnie Nationale Air France* [1975] 2 All ER 390 (folld)
5 *Administrator, Natal* v *Magill, Grant & Nell (Pty) (in liquidation)* [1967] 1 SALA 660 (folld)
6 *Re Jeavons, ex p Mackay* (1873) LR 8 Ch App 643 (folld)
7 *Re Johns; Worrell* v *Johns* [1928] Ch 737 (folld)
8 *Barclays Bank Ltd* v *Quistclose Investments Ltd* [1970] AC 567 (refd)
9 *Toovey* v *Milne* (1819) 2 B & A 683; 106 ER 514 (refd)

**Legislation referred to**

Companies Act (Cap 50, 1988 Ed) ss 280(1), 327(2)

*Jude Benny* for the plaintiff.
*Tan Hoay Djin* for the first to fourth defendants.
*Tan Chee Ming* for the fifth defendant.

*Cur Adv Vult*

**Thean J**: The plaintiff, Joo Yee Construction Co Pte Ltd, is presently in liquidation, a winding-up order having been made against it on 10 February 1989. Long before the commencement of its liquidation, that is, on 12 September 1986, the plaintiff entered into a building contract ('the main contract') with the government of Singapore ('the government') for the construction of the Blood Transfusion Services/Department of Scientific Services Complex at the General Hospital, Singapore, and International Development and Consultancy Corp Pte Ltd ('Indeco') was appointed by the government as the agent for the purpose of administering the main contract, and is the superintending officer as defined in the main contract. The first, second, third and fourth defendants ('the four defendants') are the nominated sub-contractors for the development. The provisions of the main contract governing the employment by the plaintiff of nominated sub-contractors are contained in cl 20 of the conditions of the main contract, which, so far as relevant, are as follows:

> (a) All specialists, merchants, tradesmen and others executing any work or supplying and/or fixing any goods for which prime cost prices or provisional sums are included in the specification who may be nominated or selected by the superintending officer are hereby declared to be sub-contractors employed by the contractor and are herein referred to as 'nominated sub-contractors'.
>
> (b) The superintending officer or the contractor if so instructed in writing by the superintending officer shall obtain tenders for sub-contractors' work in respect of which prime cost prices or provisional sums are included in the specification as aforesaid and the contractor shall on the written instructions of the superintending officer place such sub-contracts with the nominated sub-contractors.
>
> (c) No nominated sub-contractor shall be employed upon or in connection with the works against whom the contractor shall make what the superintending officer considers to be reasonable objection or (save where the superintending officer and contractor shall otherwise agree) who will not enter into a sub-contract on a form provided by the superintending officer providing:
>
> (i) that the nominated sub-contractor shall, in respect of the sub-contract, duly observe all the terms, stipulations and conditions herein expressed;
> (ii) ...
> (iii) that payment without discount or deduction shall be made to the nominated sub-contractor by the contractor within seven days of his receipt of the superintending officer's certificate under cl 38 hereof which includes the value of such nominated sub-contractor's work.
>
> (e) Before any such certificate is issued to the contractor he shall if requested by the superintending officer furnish to him reasonable proof that all nominated sub-contractors' accounts included in previous certificates have been duly discharged; in default whereof the government may pay the same upon a certificate of the superintending officer and deduct the amount thereof from any sums due to the contractor. Upon a certificate of the superintending officer, direct payments may also be made by the government to the nominated sub-contractors, if a petition has been presented to the court to wind up or to make bankrupt the contractor, or a receiver has been appointed to manage the affairs of the contractor, and the amount so paid shall be deducted from any sums due to the contractor. The exercise of this power shall not create privity of contract as between government and the nominated sub-contractor.

Each of the four defendants as the nominated sub-contractor on diverse dates entered into a sub-contract with the plaintiff, and the terms of each sub-contract are identical in all material respects. For my purpose, the material terms of the sub-contract are cll 22 and 26 of the conditions of sub-contract which are as follows:

> 22 The contractor shall subject to and in accordance with the main contract from time to time make application (of which prior thereto the contractor shall give to the sub-contractor at least seven days' notice unless otherwise agreed between the contractor and the sub-contractor) to the superintending officer for progress payments and for the inclusion therein of the amount which at the date thereof fairly represents the value of the sub-contract works and of any variations authorized under this sub-contract then executed and of the materials and goods delivered upon the site for use in the sub-contract works.
>
> Provided that the application shall only include the value of the said materials and goods as and from such time as they are reasonably, properly and not prematurely brought upon the site and then only if adequately stored and/or protected against weather and other casualties.
>
> The contractor shall also embody in or annex to the said application any representations of the sub-contractor in regard to such value.
>
> 26 If the contractor shall fail to make any payment to the sub-contractor as hereinbefore provided and such failure shall continue for seven days after the sub-contractor shall have given the contractor written notice of the same, then the sub-contractor may (but without prejudice to any other right or remedy) inform the superintending officer and the government may pay the same upon a certificate from the superintending officer and deduct the amount thereof from any sums due to the contractor. The exercise of this power shall not create privity of contract as between the government and the sub-contractor.

In respect of works carried out by the plaintiff and the sub-contractors at various stages of the development, certificates for payment under cl 38 of the conditions of the main contract had been issued by Indeco as the superintending officer for payments to be made to the plaintiff as the main contractor; included in the certificates were the amounts payable by the plaintiff to the nominated sub-contractors respectively for the works carried out and materials and goods supplied by them, and these amounts were set out in a list annexed to each of the certificates. Clause 38, in so far as relevant, provides:

> (a) When work to the value of the sum, referred to on page 3 hereof (or less at the discretion of the superintending

officer) has been executed by the contractor in accordance with the terms of this contract, the superintending officer shall at that time and once (or more often at the discretion of the superintending officer) during the course of each succeeding month issue to the contractor a certificate showing the estimated total value of the work done up to the date of such certificate.

...

(c) Within a number of days not exceeding that referred to on page 3 of the issue of any such certificate the employer will make a payment to the contractor in connection with the work and/or materials referred to in that certificate.

Up to the date of commencement of liquidation of the plaintiff, 19 certificates had been issued, and payment of the full amount thereunder had been made to the plaintiff. Except in respect of two certificates, namely, certificate nos 16 and 17, the plaintiff had, on receipt of the amount under each certificate, paid the amounts stated in the list (annexed to the certificate) to the respective nominated sub-contractors. In respect of certificate nos 16 and 17, though full amounts thereunder had been paid by the government to the plaintiff, the following amounts remain unpaid to three nominated sub-contractors, namely: (a) $221,1067 to the first defendant; (b) $160,160 to the third defendant; and (c) $66,878 to the fourth defendant.

Since the payment under certificate no 19, no further certificate has been issued by Indeco. The reason presumably was that winding up of the plaintiff had by then commenced. Apart from some rectification works to be done, the development has been completed, and certificates are yet to be issued for payments to be made.

The liquidators of the plaintiff took out this application for determination of the following question, namely, whether upon the true construction of cl 20(e) of the main contract, any direct payment made pursuant to the said provision by the government (through the Ministry of Health) to the four defendants would, having regard to the winding-up order being made against the plaintiff, be in contravention of s 329 of the Companies Act (Cap 50, 1988 Ed) ('the Companies Act'). On this issue, I have two observations. First, the issue does not really turn on the true construction of cl 20(e) of the main contract, but on the effect of such a clause on the liquidation of the plaintiff. Secondly, the relevant section of the Companies Act involved is not s 329, as the operation of cl 20(e) does not call for any payment to be made by the plaintiff, but payment direct by the government to the nominated sub-contractors. In my opinion, the relevant provisions of the Companies Act are s 280(1), which requires the court upon compulsory liquidation of a company to cause all its assets to be collected and applied in discharge of its liabilities, and s 327(2), which in the winding up of an insolvent company imports the same rules with regard, inter alia, to the rights of secured and unsecured creditors and debts provable as are in force under the law relating to bankruptcy in relation to the estates of bankrupt persons. Sections 280(1) and 327(2) respectively provide as follows:

280(1) As soon as possible after making a winding up order, the Court shall settle a list of contributories and may rectify the register of members in all cases where rectification is required in pursuance of this part and shall cause the assets of the company to be collected and applied in discharge of its liabilities.

327(2) Subject to section 328, in the winding up of an insolvent company the same rules shall prevail and be observed with regard to the respective rights of secured and unsecured creditors and debts provable and the valuation of annuities and future and contingent liabilities as are in force for the time being under the law relating to bankruptcy in relation to the estates of bankrupt persons, and all persons, who in any such case would be entitled to prove for and receive dividends out of the assets of the company, may come in under the wind up and make such claims against the company as they respectively are entitled to by virtue of this section.

Hence, the true issue before me (which was conceded by counsel for all the parties) is whether any direct payment to be made by the government to the nominated sub-contractors pursuant to cl 20(e) of the main contract contravenes the combined operation of ss 280(1) and 327(2) of the Companies Act. With this modification I now turn to consider the issue.

The issue, in part at least, is not untouched by authorities. There are two English decisions which have a bearing on the point. The first is the case of *Re Wilkinson, ex p Fowler*[1] where a builder entered into a contract with a local authority for the construction of sewage works, and the contract provided, inter alia, that certain machinery was to be supplied by specified firms — firms specified by the local authority — and one of the terms of the contract (cl 54) provided: '... If the engineer shall have reasonable cause to believe that the contractor is unduly delaying proper payment to the firms supplying the machinery, he shall have power if he thinks fit to order direct payment to them.' About one year after the contract was made, the builder was adjudicated a bankrupt on his own petition, and at that date the contract was nearly completed, and all the machinery had been supplied and erected. There was then due a certain sum of money to the builder and this sum was claimed by the trustee in bankruptcy. However, at that date, the builder owed to several specified firms various sums of money for the machinery supplied for the works. The engineer, pursuant to cl 54, issued two orders directing payment of two sums out of the sum due to the builder to the firms in settlement of their accounts. It was held that the power conferred by cl 54 on the engineer was not annulled or revoked by the builder's bankruptcy, and that the specified firms were entitled to be paid the respective sums certified. Bigham J held that the clause amounted to an authority given by the builder to the

engineer to dispose of money, which would otherwise come to the hands of the bankrupt, in a certain way under certain circumstances and that authority could not be withdrawn even upon bankruptcy. He said, at pp 720 to 721:

> It is an authority which, in my opinion, it was not competent for the bankrupt to withdraw, and it was never contemplated he should withdraw it; and, indeed, it is not contended on behalf of the trustee that the authority was one that could be lawfully withdrawn. It is an authority, therefore, which the bankruptcy of the contractor did not annul. I have then to see whether that authority has been properly exercised. Now what happened was this. On 3 October, after the machinery had been supplied the contractor filed his own petition and was adjudicated a bankrupt — that is to say, by his own act he put it out of his power to pay for the machinery which had been supplied to him. In my opinion that very act amounted to 'unduly delaying proper payment' of the machinery firms within the meaning of cl 54. He prevented himself, by his own misfortune no doubt, from making proper and due payment.

Later he repeated his opinion thus:

> I repeat that, in my opinion, the circumstances were such as to give the engineer power to execute the provisions of cl 54. He did so, and, as that power of authority never was revoked, in my opinion it binds the trustee in bankruptcy just as much as it would have bound the contractor himself if he had never been made a bankrupt.

The second case is *Re Tout and Finch Ltd.*[2] There, a company entered into a building contract with a borough council to build some flats and the contract incorporated the terms and conditions of the Royal Institute of British Architects form of conditions of contract. By cl 21(b) of the conditions of contract, the sums directed by the architect to be paid to nominated sub-contractors for work, materials or goods comprised in the sub-contracts were to be paid by the contractor within 14 days of receiving the architect's certificate less only the retention money which the contractor might be entitled to deduct and a cash discount. Clause 21(c) provided:

> Before any such certificate is issued to the contractor he shall, if requested by the architect, furnish to him reasonable proof that all nominated sub-contractors' accounts included in previous certificates have been duly discharged, in default whereof the employer [ie the council] may pay such accounts upon a certificate of the architect and deduct the amount so paid from any sums otherwise payable to the contractor.

The contractor, after the execution of the main contract, entered into a sub-contract with a sub-contractor nominated by the architect. By cl 11(a) of the sub-contract, the contractor, in accordance with the main contract, was to apply to the architect for certificates of payment and for inclusion therein of the amount representing the value of the sub-contract works at the time, and by cl 11(b), within 14 days of receiving a certificate from the architect, the contractor was to pay to the sub-contractor the amount certified therein less the retention money and cash discount. The work under the contract was completed, and soon thereafter the contractor went into voluntary liquidation. The architect was in a position to issue the final certificate for payment but he had not done so owing to disputes between the contractor and the sub-contractor. One of the disputes was whether the sub-contractor was entitled to a declaration that in accordance with cl 21(c) of the main contract, the council was entitled to pay to the sub-contractor the balance unpaid of the amount included in the previous certificate given in favour of the sub-contractor. Wynn-Parry J held that under cl 21(c) of the main contract, the architect had the right, before he issued the certificate, to ascertain from the contractor whether the contractor had duly discharged the amounts due to the nominated sub-contractors under the previous certificates, with the consequence that if the architect made the enquiry and found that the contractor had not made those payments, then the council had a right — the matter was one for the council to decide — to pay such accounts on a certificate being duly given by the architect and, as a mere necessary machinery, to deduct the amount so paid from any sums otherwise payable to the contractor. Accordingly, he made the declaration in favour of the sub-contractor. In arriving at this conclusion, he followed the decision of Bigham J in *Re Wilkinson, ex p Fowler.*[1]

There is also an Australian case which has a bearing on the same point: *Re CG Monkhouse Pty Ltd (in liquidation) and The Companies Act.*[3] In that case, the contractor agreed to erect a building for the owner, and under the contract, the owner was entitled to nominate sub-contractors to supply and fit materials or to execute works on the site, and the contract provided for payment to sub-contractors by the contractor out of sums included in the specification, and in default of such payment for payment to them direct by the building owner and deduction thereof from money otherwise payable to the contractor. The provisions relating to such payment were contained in cl 21, which provided:

> Where prime cost or provisional sums are included in the specification for persons to be nominated or selected by the architect to supply and fix materials or to execute work on the site:
>
> (a) Such sums shall be net and shall be expended in favour of such persons as the architect shall direct.
>
> (b) The sums directed by the architect to be paid to nominated sub-contractors for work, materials or goods comprised in the sub-contract shall be paid by the builder within seven days of receiving payment from the proprietor of any sub-contractor's account included in a certificate from the architect approving the value of such work, material or goods less only any retention money which the builder may be entitled to deduct.
>
> (c) Before any certificate is issued to the builder he shall, if requested by the architect, furnish to him reasonable proof that all nominated sub-contractors' accounts included in previous certificates have been duly discharged, in default whereof the proprietor may pay such accounts upon a certifi-

cate of the architect and deduct the amount so paid from any sums otherwise payable to the builder.

A sub-contractor was not paid by the contractor for work done on the site, in consequence of which, the owner paid the sub-contractor and deducted the amount from the next payment to the contractor. Within six months after this payment, a petition was presented for the winding up of the contractor, and upon liquidation, the liquidators sought a declaration that that payment constituted a preferential payment to the sub-contractor. Street J held that it was not preferential payment and on appeal his decision was affirmed by the Court of Appeal of New South Wales. The Australian judges approached the issue differently from the two English cases. They held that the contractor was only entitled to payment of moneys within the framework of the terms of the contract and its right to payment thereunder was subject to the right of the owner to divert payment of moneys to the sub-contractor which would otherwise be paid to the contractor. The following passage of the judgment of Street J was approved by the Court of Appeal:

> Under the building contract the builder does not become entitled to receive any money otherwise than within the framework of its terms. The builder is not, where the proprietor exercises its option under cl 21(c), in a position of having a present and enforceable right to receive money. The effect of putting cl 21(c) into the contract is to divert from the builder money which might otherwise become payable to him, and to direct that money straight to the hands of the sub-contractor. No contemporaneous act on the part of the builder enters into the exercise by the proprietor of its right of election under cl 21(c) to make payment direct to the sub-contractor.

Jacobs JA, in delivering the judgment of the Court of Appeal, said at p 240:

> This is not a case where the building owner paid the sub-contractor out of moneys which were then due or would certainly become due to the building company. If it were, then there might be much to be said for the submission made on behalf of the appellant; but it is fundamental to this case that the moneys, the subject of the claim, were not due to the builder and could not, on the terms of the contract, become due so long as cl 21(c) of the contract operated. The right of the builder to receive the certificate from the architect and his right to be paid on that certificate is governed under this contract by cl 25, and cl 2 specifically makes it clear that the builder is not entitled to any certificate or to any payment except subject to cl 21(c) of the contract.
>
> That being so, the payment made by the building owner cannot be described as a payment made out of moneys for the builder. It is a payment made out of the building owner's own moneys which, if the contract were strictly carried out, would never become due to the builder.

Reverting to cl 20(e) of the main contract, it is similar in part to those corresponding provisions of the building contracts in all these cases, and it was argued by counsel for the four defendants and also by counsel for the fifth defendant that on these authorities cl 20(e) continues to have full force and effect unaffected by the liquidation of the plaintiff and that the government may, pursuant to that clause, make payment direct to the nominated sub-contractors of the respective amounts due to them. In the submissions of both counsel, the issue was fully covered by the three authorities. On the other hand, it was argued by counsel for the plaintiff that cl 20(e) cannot operate once the liquidation of the plaintiff has supervened, as the operation of that clause would contravene the provisions of the Companies Act providing for settlement of debts and liabilities of an insolvent company and that the three cases are of doubtful authority having regard to the decision of the House of Lords in *British Eagle International Airlines Ltd* v *Compagnie Nationale Air France*,[4] to which I now turn.

The facts in that case are briefly these. The International Air Transport Association ('IATA'), a body corporate, was established by a Canadian Act of Parliament with the object of encouraging collaboration among air transport enterprises. It set up a clearing house for the benefit of those of its members who wished to use its system or facility to clear their mutual accounts inter se. Each member of the clearing house agreed that the clearing house regulations as amended from time to time should be binding on it and should be deemed to constitute a contract between the member, IATA and each of the other members for the time being of the clearing house. The regulations and rules of procedure of the clearing house set out a system for settlement of the amounts owed by each member to the other members, and vice versa, in respect of their mutual rendering of services every month. Under the scheme of the clearing house, instead of members making direct payments to each other for mutual rendering of services, appropriate debits and credits would in account with IATA be entered against or in favour of a member in respect of all its dealings with all the other members, and all debits or credits of members were to be payable or receivable through the medium of the clearing house. Each member every month would notify its claim in a prescribed form to the clearing house and the other members concerned. There was a closure every month in respect of services received and services rendered by the airlines, and on closure a balance would be struck as to the amount owed to and by each of the airlines to the clearing house. Members who were in debit must pay the sum due from them to the clearing house within seven days and the clearing house would then discharge the amount due to the members in credit within the next seven days. Under the regulations, the liability of the clearing house to members was limited to the amounts collected on their behalf from the other members in debit. If, therefore, a member in debit upon clearance failed to pay the balance due from it on the call day, the members to whom the amount in question would have been paid had no claim against the clearing house. And the regulations further provided that where the debt remained outstanding at the

date of the subsequent month's clearance, the clearing house, whilst maintaining the debt against the defaulting member, would reverse all credits made in the previous month to the creditors of that debtor so that until the delinquent debtor had settled, the outstanding debit would fall on the creditors concerned. Both the plaintiff and the defendant were members of the clearing house. During the month of October 1968, the defendant received services from the plaintiff exceeding in value those rendered by it to the plaintiff. In November 1968, the plaintiff went into creditors' voluntary liquidation and the liquidator took the view that the clearing house arrangement was not binding on him and claimed that the defendant and other airlines which were in net debit to the plaintiff in respect of businesses done between 1 September and 6 November should pay the net debit balances to him to be dealt with as part of the general assets of the plaintiff available for distribution among all its creditors and that airlines which were in net credit as against the plaintiff in respect of business done during the period should prove in the liquidation for the net balances due to them as though they were ordinary unsecured creditors. The plaintiff therefore brought an action against the defendant claiming the credit balance due to it. Both the High Court and the Court of Appeal held that the clearing house arrangement was binding on the plaintiff in liquidation, and the plaintiff had no claim against the defendant. But on appeal, the House of Lords, by a majority of three to two, held that in so far as the parties to the clearing house had by agreement contracted out of the provisions of s 302 of the Companies Act 1948 for payment of unsecured debts pari pasu, those arrangements were contrary to public policy and the general rules of liquidation prevailed over them, and that on liquidation, the plaintiff was entitled to recover payments of the sum payable to it by other airlines for services rendered by it during the relevant period and that the airlines which had rendered services to it during that period became entitled to prove in liquidation for the sums payable to them. Lord Cross of Chelsea, in delivering the majority judgment, said at p 411:

> But what Air France are saying here is that the parties to the 'clearing house' arrangements by agreeing that simple contract debts are to be satisfied in a particular way have succeeded in 'contracting out' of the provisions contained in s 302 of the 1948 Act for the payment of unsecured debts 'pari pasu'. In such a context it is to my mind irrelevant that the parties to the 'clearing house' arrangements had good business reasons for entering into them and did not direct their minds to the question of how the arrangements might be affected by the insolvency of one or more of the parties. Such a 'contracting out' must, to my mind, be contrary to public policy. The question is, in essence, whether what was called in argument the 'mini liquidation' flowing from the clearing house arrangements is to yield or to prevail over the general liquidation. I cannot doubt that on principle the rules of the general liquidation should prevail. I would therefore hold that, notwithstanding the clearing house arrangements, British Eagle on its liquidation became entitled to recover payment of the sums payable to it by other airlines for services rendered by it during that period and that airlines which had rendered services to it during that period became on the liquidation entitled to prove for the sums payable to them.

It is true that the relevant provision of the Companies Act which was considered and applied in *British Eagle*[4] is s 302 and that section applies only to voluntary winding up of companies. But by virtue of the combined operation of ss 257 and 317 of that Act, the principle of pari pasu satisfaction of unsecured liabilities of an insolvent company equally applies in compulsory winding up of companies. The position therefore would remain unchanged even if the plaintiff in that case were in compulsory liquidation. Clearly, the principle that emerged from the decision is this.

Upon liquidation of an insolvent company (whether voluntary or compulsory), subject to the rights of preferential creditors and also secured creditors, if any, its property must be applied in settlement of its liabilities pari pasu, and any contract made by the company which provides for a distribution of any of its property for the benefit of one or more of its unsecured creditors which runs counter to or seeks to vary this rule, ie any 'contracting out', is contrary to public policy, and the law as regards distribution of the insolvent's property under the insolvency legislation must prevail. Accordingly, the liquidator of an insolvent company is entitled to disregard — indeed it is obligatory on him to disregard — such a contract.

In the light of this principle, I now turn to examine cl 20(e) of the main contract. Clause 20(e) has two limbs: (i) the first limb (comprised in the first sentence) enables the government to make a direct payment to nominated sub-contractors of moneys due to them from the plaintiff and operates in the event of default by the plaintiff in showing reasonable proof that the nominated sub-contractors' accounts included in the previous certificates have been paid; and (ii) the second limb (comprised in the second and last sentence) enables the government, upon certificate of the superintending officer, to make direct payment to the nominated sub-contractors if, inter alia, a petition for the winding up of the plaintiff has been presented. In respect of both limbs, it is important to bear in mind two salient points. First, the government is under no obligation to make any payment at all to any of the nominated sub-contractors, and there is no privity of contract in any way between the government and any of them. It may elect to make payment under cl 20(e), if it so wishes. Secondly, if it does make payment of any sum thereunder to a nominated sub-contractor, that sum is one that is actually due from the plaintiff, and not from the government, to the nominated sub-contractor.

The first limb of cl 2(e) is in pari materia with the corresponding provisions of the building contracts in the

three cases, namely: *Re Wilkinson*,[1] *Re Tout and Finch Ltd*[2] and *Re CG Monkhouse Pty Ltd*.[3] As had happened in the three cases, the main contractor here, the plaintiff, has failed to pay the amounts due to nominated sub-contractors, namely, $221,067 to the first defendant, $160,160 to the third defendant and $66,878 to the fourth defendant as certified in certificate nos 16 and 17.

Now, these sums are owed by the plaintiff to the three defendants respectively: they are liabilities of the plaintiff. Therefore, if the government elects to make payment of these sums to the three defendants under the first limb of cl 20(e) and in consequence deducts these amounts from moneys due or payable to the plaintiff, it is in effect distributing to the three unsecured creditors of the plaintiff sums of money which would otherwise be paid to the plaintiff and form part of the general assets of the plaintiff available for distribution among all its creditors pari pasu. On this analysis, clearly the operation of such a contractual provision in the liquidation of the plaintiff would infringe the insolvency law providing for distribution of the insolvent's property pari pasu among its creditors'; the operation of that clause would amount to a 'contracting out' of the provisions of such insolvency law. On the authority of *British Eagle*,[4] such 'contracting out' is contrary to public policy and the liquidator is entitled, and indeed is obliged, to disregard it.

It was argued by counsel for the fifth defendant that cl 20(e) should be considered and applied in the context of the whole scheme under which the main contract and the sub-contracts were made. It is true that the main contract was made only between the government and the plaintiff, and the sub-contracts were made between the plaintiff and the respective sub-contractors. However, the respective sub-contractors were selected by the government through the agency of Indeco, and the sub-contracts they made with the plaintiff were on terms dictated by the government — they were based on the standard terms provided by Indeco. The work the sub-contractors did, and the materials and goods they supplied, under the sub-contracts enured to the benefit of the government. Under cl 22 of the sub-contract, the plaintiff is obliged, in applying for progress payments under the main contract, to include in the application the amounts representing the value of the sub-contract works and materials and goods supplied. In issuing a certificate of payment to the plaintiff, Indeco is obliged to include therein the value of work done and materials and goods supplied by the sub-contractors and payments for such work, materials and goods are made by the government to the plaintiff who in turn is obliged under the terms of the sub-contracts to pay the same to the sub-contractors. In other words, though technically and contractually the payments for the sub-contract work (including materials and goods supplied) are made by the plaintiff, the certifications and payments are in fact made by the government. In so far as payments intended for the sub-contractors are concerned, the plaintiff is no more than a conduit or channel for transmitting them from the government to the sub-contractors. On the basis of this scheme, counsel for the fifth defendant submitted that if the government elects to make direct payments to the sub-contractors under cl 20(e), such payments were made not out of any funds or moneys due to the plaintiff; they were payments made for work done and materials and goods supplied by the sub-contractors for the project, and the plaintiff is not entitled to these moneys.

I am unable to accept this argument. It ignores fundamentally the contractual relationship between the government and the plaintiff and that between the plaintiff and the sub-contractors. The main contract was made between the government and the plaintiff. All the work to be carried out and materials and goods to be supplied under the main contract were to be carried out and supplied by the plaintiff or caused and procured to be done by it, and, correspondingly, all moneys to be paid for such works done and materials and goods supplied were and are payable to the plaintiff under the main contract. Any payment of such moneys to persons other than the plaintiff can only be made with the consent or on the authority of the plaintiff, and cl 20(e) of the main contract operates as an authority from the plaintiff to the government to effect such payment direct to the nominated sub-contractors. It follows that whatever sums of money the government elects to pay to the nominated sub-contractors under cl 20(e) are moneys which would otherwise be paid to the plaintiff. As between the government and the plaintiff, they are in fact moneys payable or to be payable by the government to the plaintiff. Once they are paid to the plaintiff, the latter becomes obliged to pay them to the nominated sub-contractors. But because the plaintiff had defaulted in respect of past payments to the nominated sub-contractors, the government is under cl 20(e) entitled to exercise the authority and pay the moneys direct to the nominated sub-contractors, and if it does so elect and make the payment it then deducts those payments from sums payable to the plaintiff. These moneys paid to nominated sub-contractors and subsequently deducted from sums payable to the plaintiff are, in effect, moneys payable to the plaintiff; they represent the plaintiffs' entitlement under the main contract.

I am not disposed to follow the decisions in the three cases. In all those cases, the principle of pari pasu distribution of the insolvent's property in bankruptcy or liquidation (as the case may be) under the relevant insolvency legislation was not considered. In the case of *Re Wilkinson*,[1] Bigham J held that the relevant provisions in the main contract amounted to an authority to the building owner to make direct payment to the sub-contractor the amount due to them from the main contractor and that the authority was not revoked on the bankruptcy of the con-

tractor. He did not, however, consider further whether such an authority, if exercised, as indeed it was there exercised, would have the effect of diverting to the sub-contractors, who were the creditors of the main contractors, sums of money owed by the latter which would otherwise be paid to the trustee in bankruptcy available as part of the general assets of the bankrupt for distribution pari pasu among his creditors. Wynn-Parry J in *Re Tout and Finch Ltd*[2] followed the decision of Bigham J and also did not consider this point. Nor did the Australian judges in *Re CG Monkhouse Pty Ltd.*[3] They considered only the aspect of the contractual rights of the main contractor: that is, the contractor was entitled to payment of the moneys under the contract only with the framework of the terms, and its right to payment was subject to the right of the building owner to make direct payment to the sub-contractor and deduct the amount from sums due to the main contractor. By the same token, the plaintiff in *British Eagle*[4] under the terms of the contract it made with IATA and other members of the clearing house was bound to have its debits and credits settled through the medium of the clearing house and had no right to claim its credits from those members indebted to it for services rendered; however, it was held that such a contract upon the liquidation of the plaintiff contravened the insolvency legislation providing for pari pasu distribution of its assets to its creditors.

I am reinforced in my view by a South African case: *Administrator, Natal* v *Magill, Grant & Nell (Pty) (In Liquidation).*[5] There, the plaintiff entered into a building contract with the defendant whereby the plaintiff undertook to erect a school for the defendant. The building contract contained, inter alia, provisions for employment by the plaintiff of nominated sub-contractors and for payment to them along the line as provided in cl 20 of the main contract here. Clause 21(b) of the building contract in that case provided:

> Before the issue of any payment to the contractor he shall, if requested by the Director of Building Services, furnish reasonable proof that all nominated sub-contractors' accounts, included in previous payments to the contractor, have been duly discharged. Should the contractor be in default in respect of a payment to a nominated sub-contractor, the administrator may make a direct payment from any sums due to the contractor. The exercise by the administrator of this power shall not create privity of contract as between the administrator and the nominated sub-contractor.

Subsequently, the plaintiff went into liquidation. After the commencement of the liquidation, the defendant, in view of the fact that the plaintiff had failed to pay two nominated sub-contractors two amounts due to them respectively, acting in accordance with cl 21(b), paid to the two sub-contractors two amounts totalling R3,060.42 and then deducted them from the sum paid to the liquidator. The plaintiff acting by its liquidator instituted proceedings against the defendant for recovery of this amount; to this claim the defendant pleaded that this amount was paid direct to the nominated sub-contractors. An exception to the effect that the defendant's plea disclosed no defence was upheld and on appeal was affirmed by a majority. The appellate court refused to follow the two English cases. Ogilvie Thompson JA who delivered the judgment of the majority approached the case on the basic premise that so far as concerned payments under the building contract, the building owner was the debtor and the contractor was the creditor and in relation to the sub-contracts the contractor was, in turn, the debtor with the nominated sub-contractors as the creditors. He said at p 670:

> Now while it may, in a sense, be correct to say that, in regard to progress payments under contracts such as the one under consideration, the contractor is, in relation to moneys due by him to nominated sub-contractors, merely a conduit pipe, the legal position of course is that the creditor-debtor relationship obtains only between the contractor and the building owner on the one hand and the contractor and the nominated sub-contractors on the other hand. As regards the former of these relationships, it is, in my view, important to appreciate that, upon the contractor's failing to pay a nominated sub-contractor's due claim, the building owner is, in terms of cl 21(b), in no way obliged to pay the nominated sub-contractor direct, although he may elect to do so. Moneys due and payable by the building owner to the contractor's failing to discharge a liability due by him to a nominated sub-contractor; they only become pro tanto so reduced when the building owner exercises his election to pay the nominated sub-contractor.

He then went on to hold that at the date of liquidation, the plaintiff was unable to pay its debt in full, and said, at pp 671 to 672:

> Included among the plaintiff company's concurrent creditors were the two afore-mentioned nominated sub-contractors. Defendant's action in paying them direct, and in thereafter deducting the amount so paid from his indebtedness to the plaintiff, not only converted the two nominated sub-contractors into preferent creditors receiving payment in full, but, as is obvious, it also reduced the amount available for distribution by the liquidator amongst the general body of concurrent creditors (including the two afore-mentioned nominated sub-creditors) by the R3,060.42 so paid. Once the liquidation supervened, the two nominated sub-contractors were only entitled to receive from their debtor (plaintiff company) whatever dividend was ultimately awarded to its concurrent creditors. By paying them in full after liquidation had already supervened, the defendant thus enabled the nominated sub-contractors to receive more than they were legally entitled to claim. A creditor can, of course, always stipulate for a security; but, as indicated earlier, there was no contractual privity between the defendant and the nominated sub-contractors. In law, the latter were merely concurrent creditors of the company. Moreover, as emphasized above, the defendant was only in contractual privity with the plaintiff company; the latter was his creditor. Accordingly, although the defendant's payment to the nominated sub-contractors was made pursuant to the election conferred upon him, without apparent qualification, by cl 21(b) of the contract, the exercise of that election after liquidation had supervened disturbed both the realization and the

distribution of the plaintiff company's assets as prescribed by the law relating to liquidations.

I am in entire agreement with the analysis of Ogilvie Thompson JA and I think it is undoubtedly correct.

I now come to the second limb of cl 20(e) of the main contract. That limb goes further than the first, and what I have said, as fortiori, applies. It is expressed to arise on the commencement of the liquidation of the plaintiff and if it is invoked on that ground, it is, in my opinion, in contravention of the combined operation of ss 280(1) and 327(2) of the Companies Act. In *Re Jeavons, ex p Mackay*,[6] at p 647, James LJ said:

> ... in my opinion a man is not allowed, by stipulation with a creditor, to provide for a different distribution of his effects in the event of bankruptcy from that which the law provides. It appears to me that this is a clear attempt to evade the operation of the bankruptcy laws.

Similarly Mellish LJ said, at p 648:

> That is to say, as I understand it, a person cannot make it a part of his contract that, in the event of bankruptcy, he is then to get some additional advantage which prevents the property being distributed under the bankruptcy laws.

Further, in *Re Johns; Worrell* v *Johns*[7] where a mortgage provided for a greater benefit to enure to the mortgagee in the event of the bankruptcy of the mortgagor occurring, which did occur, Tomlin J, in declaring such a provision as bad, said, at pp 747:

> ... and that it falls exactly within the words in *Ex p Williams* (1877) 7 Ch D 138 that I have read: 'A person cannot make it a part of his contract that, in the event of bankruptcy, he is then to get some additional advantage which prevents the property being distributed under the bankruptcy laws'. I read that as meaning not only the bankruptcy cannot do that, but having regard to the position in that case of *Ex p Williams* (1877) 7 Ch D 138, the mortgagee cannot do it. He cannot make a bargain with the mortgagor which secures to him, the mortgagee, a greater advantage if the mortgagor becomes bankrupt than he would get if he does not.

In this case, the second limb of cl 20(e) does not provide the government with any additional benefit, if it is invoked by it; but it does provide for a different distribution of the property of the plaintiff which is now in liquidation from that which the law provides. On the principle of *Ex p Mackay*[6] and *Re Johns*,[7] that provision of cl 20(e) cannot bind the liquidation of the plaintiff.

Lastly, counsel for the fifth defendant submitted that moneys due to the nominated sub-contractors do not belong to the plaintiff in any event but held on trust for them. I do not see how such a trust can arise. There is clearly lacking the subject matter of the trust; there is not in the hands of the government any fund in respect of which a trust can be implied in law for the benefit of the nominated sub-contractors. The government is not holdings, nor has it earmarked, any fund for the specific purpose of making payment to the sub-contractors. It may be, and probably it is, under an obligation to make payments under the main contract; but such obligatory payments are to be made to the plaintiff. The government is under no obligation to make any payment to the sub-contractors under cl 20(e); it may elect to do so, if it wishes. If it does not elect to do so, the sub-contractors have no claim against it whatsoever. The cases of *Barclays Bank Ltd* v *Quistclose Investments Ltd*[8] and *Toovey* v *Milne*[9] are wholly irrelevant and are of no assistance here.

In the result, in my judgment, if cl 20(e) of the main contract is invoked, it would in the circumstances contravene the combined operation of ss 280(1) and 327(2) of the Companies Act; the liquidator is not bound by that clause, and consequently any payment made thereunder to the sub-contractors is void as against him.

I was told that the parties have agreed between themselves on the question of costs, and accordingly I make no order thereon.

*Order accordingly.*

Solicitors: *Joseph Tan Jude Benny & Co*; *Tan Lee & Choo*.

Reported by *Kevin Mathews*

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## Kian Choon Investments (Pte) Ltd v Societe Generale & Anor

HIGH COURT (SINGAPORE) — SUIT NO 1618 OF 1989
THEAN J
15 JANUARY 1990

*Land Law — Mortgage — Mortgagee's duty in sale of secured land — Sale by mortgagee with option to repurchase*

*Banking — Mortgage — Duty of mortgagee in selling mortgaged property*

*Civil Procedure — Interim injunction — Mortgagee's sale of land — Whether damages adequate remedy*

The plaintiffs are the owners of the land and premises with a building thereon known as 'The Octagon' ('the property'). They executed two mortgages respectively in favour of the first defendants ('the bank') to secure banking facilities. The plaintiffs were in default under the mortgages, and the bank appointed receivers to receive the rents and profits of the property. Eventually, the parties came to an amicable settlement, embodied in a deed of compromise. In so far as the property is concerned, the deed of compromise provided, inter alia, that possession thereof was to be delivered to the bank subject to existing tenancies and conferred on the bank certain rights. Accordingly, the bank took possession of the property as mortgagee. The bank initiated steps to sell the property as mortgagee and later agreed to sell the property to Amcol, the second defendant. Two terms of this agreement are material. Amcol granted to the bank a lease of four